

## Message Text

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ACTION EUR-12

INFO OCT-01 ISO-00 CIAE-00 DODE-00 PM-05 H-01 INR-07  
L-03 NSAE-00 NSC-05 PA-01 PRS-01 SP-02 SS-15  
USIA-06 AID-05 CEA-01 COME-00 EB-08 EA-10 FRB-03  
IO-13 NEA-10 OPIC-03 TRSE-00 LAB-04 SIL-01  
AGRE-00 OMB-01 /118 W  
-----013280 230826Z /12

R 230650Z AUG 77  
FM AMEMBASSY HELSINKI  
TO SECSTATE WASHDC 1767  
INFO AMEMBASSY COPENHAGEN  
AMEMBASSY OSLO  
AMEMBASSY PARIS  
AMEMBASSY STOCKHOLM

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E.O. 11652: N/A  
TAGS: ECON, FI  
SUBJECT: AGRICULTURAL INCOMES NEGOTIATIONS AND POSSIBILITY  
OF SWEDISH DEVALUATION THREATEN FRAGILE ECONOMIC POLICY  
CONSENSUS

1. SUMMARY. AS THE SUMMER SEASON ENDS, FINLAND IS MIRED  
IN ITS THIRD YEAR OF NO GROWTH, AND UNEMPLOYMENT AND INFLATION  
REMAIN STUBBORNLY HIGH. MOREOVER, THE GOVERNMENT FACES  
TWO IMMINENT THREATS TO THE FRAGILE CONSENSUS BEHIND ITS  
MILDLY ANTI-INFLATIONARY INCOMES AND FISCAL POLICIES. THE  
DEMANDS OF THE CENTRAL ASSOCIATION OF AGRICULTURAL PRODUCERS  
(MTK) IN FARM INCOMES NEGOTIATIONS NOW UNDER WAY WOULD  
REQUIRE EITHER ADDITIONAL INFLATIONARY AGRICULTURAL SUBSIDIES,  
INTENSIFYING THE GOVERNMENT'S CURRENT REVENUE SHORTAGE,  
OR AT LEAST EQUALLY INFLATIONARY AGRICULTURAL PRICE  
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INCREASES STRONGLY OPPOSED BY LABOR. SWEDISH DEVALUATION  
WOULD PROBABLY FORCE A FINNISH DEVALUATION AND RENEGOTIATION  
OF LAST SPRING'S TWO-YEAR INDUSTRIAL WAGE AGREEMENTS.  
END SUMMARY.

2. REAL GDP DURING THE FIRST HALF OF 1977 DECLINED  
SLIGHTLY TO APPROXIMATELY THE 1974 LEVEL. WHILE IT

SHOULD RISE OVER THE SECOND HALF OF THE YEAR TO AROUND LAST YEAR'S SECOND-HALF LEVEL, THE MINISTRY OF FINANCE ESTIMATES THAT THE GAIN OVER THE THREE-YEAR PERIOD 1975-1977 WILL BE ONLY TWO TO THREE PERCENT. WITH CYCLICAL RECOVERY OF FINLAND'S WESTERN EXPORT MARKETS SLACK AND UNSTEADY, THE MINISTRY'S ECONOMICS DEPARTMENT HAS BACKED OFF MORE OPTIMISTIC EARLIER FORECASTS A YEAR AGO OF AN EXPORT-LED RECOVERY BEGINNING LATE THIS YEAR, AND ADMITS RECOVERY IS NOT YET IN SIGHT. WOOD PRODUCT EXPORTS SHOW SCATTERED SIGNS OF MODEST RECOVERY: LUMBER PRICES HAVE RISEN AND THE VOLUME OF PAPER EXPORTS IS RISING SLIGHTLY, THOUGH PRICES REMAIN DEPRESSED IN THE FACE OF LARGE INVENTORIES. PROSPECTS FOR FINLAND'S OTHER MAJOR EXPORT SECTOR, THE METAL AND ENGINEERING SECTOR, ARE GLOOMIER. ORDERS CONTINUE TO FALL, ESPECIALLY IN THE GLOBALLY DEPRESSED SHIPBUILDING INDUSTRY, AND PRESSURES GROW FOR EXTENSION OF GOVERNMENTAL SUBSIDIES TO ORDERS BY DOMESTIC SHIPPERS. NEXT YEAR SHIPYARDS WILL HAVE TO LAY OFF AT LEAST 2,000 WORKERS, OVER TEN PERCENT OF THEIR LABOR FORCE. UNEMPLOYMENT IN FINLAND IS 25 PERCENT HIGHER THAN A YEAR AGO. OVER THE PERIOD 1975-1977 EMPLOYMENT WILL HAVE FALLEN OFF BY AROUND FIVE PERCENT.

3. TRENDS IN THREE OTHER AREAS--BALANCE OF PAYMENTS, INFLATION, AND SPENDING PATTERNS--ARE LESS GLOOMY. THE LIMITED OFFICIAL USE

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TRADE DEFICIT FOR THE FIRST HALF OF 1977 WAS FMK 641 MILLION (\$161 MILLION) COMPARED WITH FMK 1,673 (\$418 MILLION) FOR THE FIRST HALF OF 1976. IMPORTS OF CAPITAL EQUIPMENT, AND TO A LESSER EXTENT, OF CONSUMER GOODS, HAVE FALLEN OFF. BANK OF FINLAND OFFICIALS ARE PRIVATELY CONFIDENT THAT THE CURRENT ACCOUNT DEFICIT FOR THIS YEAR WILL BE KEPT COMFORTABLY UNDER THEIR TARGET OF FMK 1.5 BILLION (\$375 MILLION) COMPARED WITH FMK 4.4 BILLION (\$1.1 BILLION) LAST YEAR. THEY ADMIT, HOWEVER, THAT ONCE THE LONG-AWAITED RECOVERY DEVELOPS THE LARGE FOREIGN DEBT THAT HAS ACCUMULATED (FMK 23 BILLION OR \$5.75 BILLION) WILL REQUIRE CONTINUED RESTRAINTS ON IMPORTS OF CAPITAL GOODS WHICH WILL HAVE MORE BITE AS DEMAND PICKS UP.

4. INFLATION HAS REMAINED HIGH - THE CPI CLIMBED EIGHT PERCENT DURING THE FIRST HALF OF 1977 COMPARED WITH 11.8 PERCENT DURING ALL OF 1976 - BUT A TWO-PERCENT INCREASE IN TURNOVER TAX, THE 5.7 PERCENT DEVALUATION ON APRIL 4, AND HIGHER RAW MATERIALS PRICES ACCOUNTED FOR MUCH OF THE INCREASE. LAST SPRING'S WAGE AGREEMENTS, THOUGH INCORPORATING INCREASES RUNNING AT ABOUT SEVEN

PERCENT THIS YEAR AND NINE PERCENT NEXT YEAR, REPRESENT  
A TACIT ACCEPTANCE BY LABOR OF SOME REDUCTION IN REAL  
INCOME, TAKING INTO ACCOUNT EXPECTATIONS BASED ON  
PRICE TRENDS OVER RECENT YEARS.

5. MODERATION OF INCREASES IN GOVERNMENT SPENDING IS  
ALSO BEING ACCEPTED TACITLY. MINISTRIES' SUBMISSIONS  
FOR THE BUDGET TO BE TABLED IN PARLIAMENT ON  
SEPTEMBER 8 ARE REPORTED TO BE MORE REALISTIC THAN  
IN PREVIOUS YEARS. INDICATIONS OF CONSUMER BELT-  
TIGHTENING ALSO ARE BEGINNING TO SHOW UP, IN A TEN-  
PERCENT DECLINE IN WHOLESALE TRADE IN CONSUMER GOODS IN  
THE FIRST HALF OF THE YEAR, AND IN DECLINING CONSUMPTION  
OF GASOLINE AND THE MORE EXPENSIVE MEAT AND DAIRY PRODUCTS.  
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ALTHOUGH THE COMMUNISTS CALL FOR COMBATTING THE RECESSION THROUGH STEPS TO INCREASE PERSONAL INCOME AND EMPLOYMENT, BOSERVERS ON THE CENTER AND RIGHT BELIEVE THAT RESTORATION OF ECONOMIC EQUILIBRIUM WILL REQUIRE GUT ADAPTATION TO HARD TIMES THAT WOULD BE REFLECTED IN CURTAILMENT OF EXPANSION OF THE GOVERNMENTAL SECTOR AND OF CONSUMER SPENDING. SUCH ATTITUDINAL CHANGES COME HARD IN FINLAND BECAUSE OF HISTORICAL TENSIONS OVER DIVISION OF POWER AND INCOMES AMONG INDUSTRY, LABOR, AND AGRICULTURE. IT IS HERE THAT THE GOVERNMENT SEEMS TO HAVE MADE FRAGILE BUT VITAL PROGRESS OVER THE PAST YEAR.

6. THE CURRENT AGRICULTURAL INCOMES NEGOTIATIONS INVOLVE AN MTK CLAIM OF FMK 683 MILLION (\$171 MILLION) FOR COMPENSATION FOR PRODUCTION COST INCREASES AS WELL AS FOR LIMITED OFFICIAL USE

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INCOME INCREASES PROPORTIONAL TO THOSE RECEIVED BY LABOR IN THE SPRING INDUSTRIAL WAGE NEGOTIATIONS. IT WOULD BE EXTENDED BY RAISING AGRICULTURAL TARGET PRICES OR INCREASING ALREADY EXTENSIVE AGRICULTURAL SUBSIDIES.

7. PEKKA OIVIO, CHAIRMAN OF SAK (CHAIRMAN OF THE CENTRAL ASSOCIATION OF FINNISH TRADE UNIONS), STATED RECENTLY THAT IN THE AUTUMN INDUSTRIAL INCOMES REVIEW IT WILL BE DIFFICULT TO AVOID INCREASED DEMANDS IF THE AGRICULTURAL INCOME NEGOTIATIONS RAISE CONSUMER PRICES. HOWEVER, MINISTER OF AGRICULTURE AND CENTER PARTY CHAIRMAN VIROLAINEN HAS STATED THAT AN INCREASE IN CONSUMER PRICES CANNOT BE AVOIDED, SINCE THE GOVERNMENT DOES NOT HAVE FUNDS TO COMPENSATE AGRICULTURE THROUGH INCREASES IN SUBSIDIES. PAUL PAAVELA, SDP MINISTER OF FINANCE, HAS STATED THERE IS NO POSSIBILITY OF EXTENDING ADDITIONAL SUBSIDIES, AND INDEED THE GOVERNMENT IS CURRENTLY POSTPONING ALL BUT OBLIGATORY PAYMENTS BECAUSE OF A TEMPORARY REVENUE SHORTAGE. LAST WEEKEND PRIME MINISTER SORSA TOOK THE LINE THAT THE PRESENT GOVERNMENT IS NOT BOUND BY AN UNPUBLISHED UNDERSTANDING APPARENTLY ARRIVED AT DURING THE NEGOTIATIONS LAST SPRING UNDER THE PREVIOUS GOVERNMENT THAT FMK 155.4 MILLION (\$39 MILLION) IN AGRICULTURAL COST INCREASES FOR WHICH COMPENSATORY TARGET PRICE INCREASES WERE NOT THEN NEGOTIATED WOULD BE MADE UP IN THE FALL. THE CENTER PARTY AND VIROLAINEN HAVE NOT YET REACTED PUBLICLY TO SORSA'S STATEMENT. FROM THE FOREGOING IT IS OBVIOUS THAT THE AGRICULTURAL INCOMES NEGOTIATIONS POTENTIALLY COULD POSE A SERIOUS PROBLEM FOR THE INTERNAL COHESION OF THE SORSA GOVERNMENT, WHICH SEEKS TO BALANCE THE DEMANDS OF THE AGRICULTURAL SECTOR, IDENTIFIED IN THE GOVERNMENT

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COALITION MOST CLOSELY WITH THE CENTER PARTY, AND THE CONCERNS OF LABOR, WHOSE INTERESTS THE SDP AND SKDL REPRESENT IN THE GOVERNMENT. THE SORSA GOVERNMENT IS COMMITTED BOTH TO PROTECTING AGRICULTURAL INCOME AND TO AVOIDING PRICE INCREASES THAT WOULD REOPEN LAST SPRING'S COLLECTIVE LABOR AGREEMENTS. AT THIS POINT NEITHER THE OUTCOME OF THE NEGOTIATIONS NOR THE EFFECTS ON THE GOVERNMENT'S ECONOMIC POLICY LINE AND RELATIONS BETWEEN THE CENTER PARTY AND SDP ARE PREDICTABLE.

8. A SECOND MAJOR UNSETTLING DEVELOPMENT THAT COULD ARISE SHORTLY IS A SWEDISH DEVALUATION. THE BANK OF FINLAND'S KEY FOREIGN OPERATIONS OFFICIAL SAID PRIVATELY LAST WEEK THAT WITH SPECULATIVE PRESSURES MOUNTING HE THOUGHT THE SWEDES LIKELY TO DEVALUE WITHIN THREE WEEKS. THE BANK WOULD THEN CLOSE ITS FOREIGN OPERATIONS FOR A COUPLE OF DAYS, HE PREDICTED, AWAITING NORWEGIAN AND DANISH REACTIONS. OUR VIEW IS THAT THE BANK AND GOVERNMENT WOULD HAVE NO CHOICE BUT TO DEVALUE THE FINNMARK. WHILE A DEVALUATION THAT SUCCEEDED IN DAMPENING INFLATIONARY REPERCUSSIONS WOULD WORK TO FINLAND'S ADVANTAGE IN RESTORING INTERNATIONAL COMPETITIVENESS, IT APPEARS LIKELY THAT LABOR WOULD PRESS FOR RENEGOTIATION OF LAST SPRING'S WAGE AGREEMENTS, WHICH CONTAIN CLAUSES NULLIFYING THEM IN EVENT OF MAJOR DEVALUATION. DEVALUATION, NO LESS THAN INCOMES ISSUES, RAISES SENSITIVE SECTORAL ALLOCATIONAL PROBLEMS.

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## Message Attributes

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